Stabilizing the TRS Fund: Exploring the Alternatives

The Montana Teachers' Retirement System has a $1.8 billion unfunded liability.

Current statutory contribution rates already fund two-thirds of that liability, leaving a shortfall of about **$633 million.**

Based on the 2011 actuarial valuation, this represents a **3.53%** gap between current contribution rates and being actuarially funded over a 30-year amortization period. That's about $60 million for the 2015 biennium.

How to erase that 3.53% shortfall?
- Increase contribution rates,
- Reduce benefit rates,
- Secure a new source of revenue, or
- Find a workable combination of all three.

The challenge for Montana is far less dire than in Rhode Island, Illinois, or California. Those states are just now tackling issues that Montana addressed years ago. However, unless the 2013 Legislature enacts corrective measures, the unfunded liability will grow, doubling in the next 20 years, and the TRS pension fund will run out of money by 2055.

Prudent, relatively small changes now can avert the need for more drastic measures later.

Changes can be phased in to avoid harming those nearing retirement. The system can also be made more resilient to financial and demographic trends.

Moving to a Defined Contribution plan would increase costs and do nothing to address the shortfall.

Based on strategies adopted in other states, TRS has identified the following alternatives for consideration as we explore ways to pay down the unfunded liability. Actuaries Cavanaugh MacDonald, LLC, calculated the impact each alternative would have on reducing TRS's current 71-year amortization period and 3.53% funding shortfall (as of July 1, 2011). **These effects are not necessarily additive.** Also, as time passes, the actual numbers may change due to market gains or losses and other factors. Nevertheless, the information given here provides a reasonable basis for weighing the alternatives.

Alternative	Existing Plan	Change to:	Reduces Amortization By:	Reduces Shortfall By:
Raise Employee Contribution Rate	7.15%	7.65% (+0.5%)	10 years	0.37%
		Or 8.15% (+1.0%)	18 years	0.81%
Raise Employer Contribution Rate	7.47%	8.47% (+1.0%)	22 years	1.0%
Raise State General Fund Rate	2.49%	3.49% (+1.0%)	22 years	1.0%
Raise Average Final Compensation	3 years	5 years	18 years	0.91%
Reduce Multiplier	1.667%	1.50%	31 years	2.17%
Reduce Guaranteed Annual Benefit Adjustment	1.50%	1.25%	9 years	0.39%
Raise Vesting	5 years	10 years	3 years	0.10%
Raise Early Retirement	Age 50 & 5 yrs	Age 55 & 5 yrs	1 year	0.05%
Raise Regular Retirement	Age 60 w/5 yrs, or 25 yrs	Age 60 w/5 yrs, or 30 yrs	17 years	0.87%
		Or Age 65 w/5 yrs, or 30 yrs	30 years	1.94%

Montana Teachers' Retirement System

Far from needing an immediate and staggering infusion of taxpayer dollars, the TRS fund can be righted with more prudent, gradual, and relatively small adjustments.

The 3.53% shortfall can be made up through a combination of contribution increases, benefit reductions, changes to plan elements, and new funding sources.

Moving to a Defined Contribution 401(k)-style plan only makes the situation worse. It would:

- Do nothing to pay down the unfunded liability
- Increase costs to the state
- Reduce retirement security for employees
- Impair recruitment and retention of the best career-minded people

The sooner we make adjustments, the better the outcome will be for everyone—teachers, retirees, employers, and taxpayers.

TRS By the Numbers

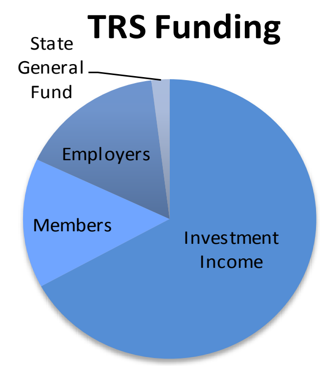
$2.9 billion in current assets

7.9% annual real rate of investment return over the last 17 years

$249 million in benefits paid annually

$24,785 average annual retirement benefit

$5 to $7 in economic activity generated by every benefit $1



Employer (taxpayer) contributions to state and local public pensions are just 2.27% of all state and local government spending in Montana.

Possible Changes to New Hires — Creating a Two-Tier Plan

To stabilize long-term funding, other states have adjusted contribution and benefit rates and modified other plan elements for new hires. Possible changes include:

- Increase employee contribution rate
- Increase employer contribution rate
- Increase state contribution rate
- Raise Average Final Compensation from 3 to 5 years
- End 25-year retirement at any age
- Set regular retirement on a "rule of 90" where age and years of service sum to 90.
- Raise regular retirement to age 65
- Raise early retirement to age 55 w/5 years of service
- Change the multiplier (currently at 1.667%)
- Increase vesting period
- Suspend or reduce cost-of-living adjustments

Changes to new hires can make the system more cost-efficient over the long term. But changes to new hires alone are not enough to pay down the unfunded liability before TRS runs out of money.